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UNCLAS SECTION 01 OF 02 SHANGHAI 000117

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SUBJECT: COSCO LIANYUNGANG SHIPYARD DETERMINED TO EXPAND DESPITE
SHIPPING INDUSTRY WOES

REF: BEIJING 443

(U) This message is sensitive but unclassified.

11. (SBU) Summary: COSCO (Lianyungang) Shipyard Co., Ltd. (hereinafter CLYGS) has benefitted from Lianyungang's ocean-front location and central and local government support. Due to the economic downturn, business has not kept up with expectations, leaving unused service capacity. In spite of the disappointing numbers, CLYGS plans to move forward beyond original repair and conversion operations and expand to shipbuilding operations. End summary.

12. (SBU) As part of a March 2-4 reporting trip to Lianyungang in the north of Jiangsu Province, Consulate Econoffs met with managers and toured operations at COSCO (Lianyungang) Shipyard Co., Ltd. (CLYGS)CLYGS. CLYGS managers said they have consistently received cooperation and support from local officials. They were pleased to reciprocate that support by assembling their senior managers to meet their U.S. Consulate visitors in response to a same-day request from the Lianyungang Foreign Affairs Office. (A previously confirmed visit to a different Lianyungang shipyard was hastily cancelled at mid-day due a major traffic accident which had blocked an access road.)

13. (U) CLYGS is a subsidiary to COSCO Shipyard Group, the second largest shipyard group in the world, which is also a state-owned enterprise. Located on prime Lianyungang harbor-front property, the CLYGS subsidiary mainly repairs and offers conversion design and execution services to vessels for bulk or offshore oil industry use. Senior management included a team of well-trained staff transferred from other major COSCO shipyards in China including Dalian, Nantong, Shanghai, and Guangzhou. According to Tian Jun, CLYGS Executive Deputy General Manager and Party Committee Secretary, the firm' leaders have multi-lingual fluency due to their frequent interactions with their internationally-sourced customer base. Ships home-ported in India, Norway, and Taiwan were berthed for CLYGS services at the

time of our visit.

A Large Presence on the Lianyungang Waterfront

¶4. (U) Operations at CLYGS only commenced in March 2008. With a production site measuring 220,000 square meters, one floating dock, and three berths, CLYGS is capable of annually serving 60 vessels of various types. The company is situated on prime deep-waterfront property which allows easy berth and launching access from ocean-going vessels. Ship conversions, such as making oil tankers double-hulled to comply with International Maritime Organization requirements or converting tankers to bulk carriers, is the largest revenue-generating part of CLYGS operations. At full capacity, CLYGS can service up to nine vessels at a time. One year after its opening, CLYGS currently employs approximately 3,000 workers, servicing 24-hour operations.

Environmental Considerations

¶5. (SBU) When asked to describe the environmental impact awareness programs CLYGS employs, Tian asserted that CLYGS puts high importance on control of environmental degradation. CLYGS is located close to the Lianyungang city center and particular attention has been placed on the company's impact on the local population concentrated nearby, he said. (Comment: Even so, during the tour of CLYGS facilities, employees were seen sandblasting hull paint into the water off a large bulk vessel berthed on the floating dock, and shortly after, while driving

SHANGHAI 00000117 002 OF 002

near the perimeter of CLYGS operations, Econoff noticed deposits of paint-laced sludge collecting along the shoreline. End comment.)

Good Local and Central Government Relations

¶6. (SBU) Central government leaders have encouraged expansion of port activity in Lianyungang, and General Secretary Hu Jintao specifically addressed development of Lianyungang during the 17th CPC meetings at the end of 2007, Tian explained. He said that the local government has been very supportive of CLYGS in the past, and CLYGS expects a continuation of support from the local and central governments. The Lianyungang Municipal Government has offered free training on port and shipping operations for CLYGS workers, who hail from all over China, for example. Although CLYGS will not receive funds from China's economic stimulus plan directly until CLYGS begins shipbuilding operations sometime in the future, Tian said, stimulus funds will benefit COSCO operations and will in turn help CLYGS indirectly. The CLYGS managers, as well as Lianyungang Municipal Government officials with whom we met, expect that Chinese economic stimulus funds will include expenditures on Lianyungang harbor dredging and expansion of container terminals. Any initiatives that increase ship traffic to Lianyungang benefits CLYGS, Tian and his colleagues said, by bringing more potential customers to CLYGS's waterfront.

Expansion Plans Not Hindered by Economic Downturn

¶7. (SBU) Pending government approvals which CLYGS expects in June 2009, CLYGS will expand its waterfront presence and vessel services despite the economic downturn. Expansion plans will double service facilities with the addition of two new floating docks and two adjoining berths. Tian claims that the expansions, once approved, will double CLYGS's repair and conversion capacity in six to eight months time. After the expansion, CLYGS will also diversify its business operations

beyond repair and conversion by adding construction of jack-up rigs and specialty vessels that require complex engineering and fabrication and are likely to have higher profit margins than building of more common ocean-going commercial vessels. CLYGS remains confident about its future business development in Lianyungang, planning expansion step-by-step as economic conditions warrant.

Impact of Economic Crisis

18. (SBU) CLYGS management noted that business volume has been affected by the world-wide economic downturn. Many clients have rescheduled maintenance orders, and at the time of the March 3 visit, only four ships were berthed for CLYGS services, below company projections of servicing up to nine vessels at any given time. Tian said payments from customers have become more difficult than normal to obtain. He also allowed that winter press reports indicating dozens of cancelled orders for new ships in Chinese shipyards could be true, but stressed that CLYGS has had no outright cancellations of any of its repair and conversion work during its first year of operations.

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